Fiscal Note 2009 Biennium

GOVERNOR'S OFFICE OF BUDGET AND PROGRAM PLANNING

Bill #	HB0833		**Title:**	20-20 tax plan -- school mills income tax credit and increase exemption amount
Primary Sponsor:	Stahl, Wayne		**Status:**	As Amended in Senate - Revised

- ☑ Significant Local Gov Impact
- ☑ Needs to be included in HB 2
- ☑ Technical Concerns
- ☐ Included in the Executive Budget
- ☐ Significant Long-Term Impacts
- ☐ Dedicated Revenue Form Attached

FISCAL SUMMARY

	FY 2008 Difference	FY 2009 Difference	FY 2010 Difference	FY 2011 Difference
Expenditures:				
General Fund	$101,809,620	$1,112,851	$715,296	$733,180
State Special Revenue	$298,077	$303,010	$310,768	$318,677
Other	$24,000	$0	$0	$0
Revenue:				
General Fund	$507,171	$6,400,727	$7,654,871	$9,914,664
State Special Revenue	$224,822	$107,515	$106,775	$105,822
Net Impact-General Fund Balanc	($101,302,449)	$5,287,876	$6,939,575	$9,181,484

Description of fiscal impact: This legislation provides tax relief and increases tax compliance through a variety of provisions.

HB529, HB680, and HB833 Tax Package -- 2007 Legislative Session

Balance Sheet

FY 2008 - 2009	**($111,472,347)**
FY 2010 - 2011	**($12,348,409)**

Resident Taxpayers	Nonresident Taxpayers	Page #	Title	GF Impact 2008 - 2009	GF Impact 2010 - 2011
0%	100%	p. 7-9	Abusive tax shelters and non-resident withholding on land sales	$26,166,065	$30,251,944
0%	100%	p. 17	Revise tax treatment of income and dividends of real estate investment trusts	$13,233,123	$19,577,280
0%	100%	p. 3	Prevent corporations from channeling income to insurance subsidiary	$4,500,000	$4,500,000
20%	80%	p. 5	Withholding for natural resource royalty payments	$3,419,195	$4,739,960
10%	90%	p. 20	Five year statute of limitations for corporation license tax	$2,894,550	$3,859,400
0%	100%	p. 19	Revise water's edge tax law	$2,600,000	$5,200,000
50%	50%	p. 11	Improved exchange of information and compliance	$2,224,927	$2,432,635
0%	100%		Revise tax laws to authorize department of revenue to collect out-of-state debt - in **HB680** (passed both Houses)	$892,921	$891,779
2%	98%	p. 9-11	Revise lodging and sales and use tax to end unfair competition by internet lodging sellers against MT lodging businesses	$636,105	$653,542
100%	0%	p. 3	Withholding on lump sum retirement distributions	$297,150	($2,850)
20%	80%	p. 18	Secretary of state - Department of Revenue taxpayer identification	$0	$0
0%	100%	p. 18	Make grantor trusts pass-through entities for tax withholding and reporting	$0	$0
			Total	$56,864,036	$72,103,690

Resident Taxpayers	Nonresident Taxpayers	Page #	Title	GF Impact 2008 - 2009	GF Impact 2010 - 2011
100%	0%	p. 4	$400 property tax rebate	($95,953,736)	$0
100%	0%	p. 17	Homeowner/Renter Credit	($30,539,918)	($30,539,918)
91%	9%		Local government and school reimbursement for Class 8 Exemption **(HB529)**	($16,384,910)	($29,369,548)
50%	50%	p. 11	Loss of revenue from reduced penalties	($8,373,750)	($8,883,712)
100%	0%	p. 20	Revise energy conservation and weatherization laws	($6,115,404)	($7,430,317)
100%	0%	p. 5	Renters' tax credit	($6,022,222)	$0
91%	9%	p. 14	General Fund Cost of Class 8 Exemption	($4,163,891)	($6,442,910)
100%	0%	p. 21	35 mpg vehicle fee exemption	($782,551)	($1,785,693)
			Total	($168,336,382)	($84,452,098)

FISCAL ANALYSIS

<u>Assumptions:</u>

Withholding from Early Retirement Fund Withdrawals

1. Distributions from tax-deferred accounts such as IRAs, retirement funds, and deferred compensation accounts are subject to federal and state income tax. Under current law, when an individual makes certain types of lump-sum withdrawals from a tax-deferred account, the account manager is required to withhold 20% of the amount withdrawn to cover the recipient's federal income tax liability. There is no corresponding requirement to withhold for Montana income taxes.
2. Section 1 would require account managers to withhold 30% of any amount withheld for federal taxes to cover the recipient's Montana income tax liability for distributions made after December 31, 2007. No state withholding would be required if the recipient elects to have no federal withholding.
3. This bill would not change income tax liability and would have a very small effect on the amount of income tax collected.
4. Each year, taxpayers who receive lump-sum distributions and do not keep funds to pay the tax on the distribution have about $300,000 in income tax liability that they are unable to pay in full when they file their next return. Most of these taxpayers do pay their tax, but end up paying it late, often in installments.
5. With withholding, about $300,000 in taxes that would have been paid in later years would be paid in the year they are due. This would results in $300,000 of additional revenue in CY 2008, split evenly between FY 2008 and FY 2009, but no change in revenue in later years.
6. Employment in Montana is approximately 436,000. Nationally, 63% of employees are covered by some type of pension plan. From 2000 through 2005, the Montana Public Employee Retirement System had an average ratio of lump sum disbursements to active members of 10.8%. This gives an estimate of the number of annual Montana lump sum disbursements of 29,665 (436,000 x 63% x 10.8%). In about half of disbursements, funds will be rolled over to another tax-deferred account or the recipient will elect to forgo withholding. Thus, the Department of Revenue will process about 15,000 withholding statements and payments each year. Additional general fund operating costs would be $1,425 per year in FY 2008 and FY 2009, increasing by 2.5% in FY 2010 and FY 2011.

Insurance Stuffing

7. Under current law, insurance companies are taxed under the state's premiums tax instead of the state's franchise or income tax. Under the premiums tax rules, certain gains on assets held by insurance companies and dividend payments from fully-owned insurance subsidiaries are not subject to tax. This preferential tax treatment is intended to provide stability to the insurance industry and ensure that insurance companies have sufficient asset growth to cover claims. The preferential tax treatment is unique to insurance companies and is not intended for use by non-insurance corporations. Other types of corporations are subject to the corporate income tax.
8. This legislation will not change the preferential tax treatment given to insurance companies. Instead, Sections 2 through 8 prorate the dividends deduction that can be claimed by non-insurance parent companies on assets transferred to the insurance affiliate. The dividend deduction will be prorated by the capitalization percentage, which is based on the ratio of the premium income to total income of all insurance companies in the commonly-controlled group. A high ratio of premium income to total income indicates the insurance company is predominately involved in the insurance business, and is not serving as a tax shelter.
9. This legislation also restricts the dividends-received deduction for any dividends attributable to premiums received by the insurance company from a member of the insurance company's commonly-controlled

group. This provision ensures affiliated corporations are not paying excessive premiums to the insurance company in order to increase the capitalization percentage, thus increasing the deduction allowed.

10. The proposed legislation limits interest or expense deductions on property transferred to the insurance company by the non-insurance parent corporation for the purpose of tax-free accumulation of investment income. Further, transfers of appreciated property to an insurance company affiliate are recognizable and taxable gains in certain circumstances.
11. Finally, the proposed legislation restricts excessively-overcapitalized insurance companies from receiving preferential tax treatment by including the insurance affiliate's share of investment income, minus premiums-received income, in the non-insurance company parent's gross income if the insurance affiliate has less than 10% of its income from premiums.
12. These provisions apply to tax years beginning after December 31, 2006.
13. The Department of Revenue (DOR) has identified 2-4 companies that will likely be subject to additional tax liability upon passage of this bill. The estimated liability increase per company is between $500,000 and $1 million.
14. DOR estimates the fiscal impact of this legislation is $2.250 million in each fiscal year it is fully implemented, assuming 3 companies will be subject to an additional assessment of $750,000.
15. Corporate license tax returns are due on or before the 15th day of the fifth month after the end of the tax year. However, an automatic six-month extension is available for corporations, if requested, and additional extensions can be requested. Corporations reporting on a fiscal year basis, whose fiscal year begins December 1, would not be required to file until April 15th. With the automatic six-month extension the due date for the return is October 15th. Therefore, a corporation whose fiscal year began December 1, 2006 would not be required to file until October 15, 2008, which is in FY 2009. Corporations are responsible for making quarterly estimated payments which must be either 80% of the total tax shown on the return for the taxable year, or 100% of the total tax for the prior taxable year. For the purposes of this fiscal note, it is assumed that additional revenue from one of the three corporations projected by DOR to be subject to additional tax liability will be paid beginning in FY 2009. The additional revenue from the other corporations is assumed to be paid beginning in FY 2008. Therefore, revenue for FY 2008 will be $1.5 million ($2.250 million – $0.750 million); FY 2009 revenue will be $3.0 million ($2.250 million + $0.750 million); and FY 2010 and FY 2011 revenue will be $2.250 million.
16. DOR will not incur any additional expenses due to passage of this legislation.

Property Tax Refund

17. Sections 9 through 11 provide owners of a primary residence in Montana a rebate on tax year 2004, tax year 2005, and tax year 2006 property taxes assessed and paid up to a maximum rebate amount of $400.
18. Based on figures from the 2005 American Community Survey, there are 254,458 owner-occupied houses in Montana.
19. Because this bill allows any residential owner to qualify if they paid $400 in total taxes on their residence over a three-year period, it is assumed all of the estimated 254,458 owner-occupied homeowners will qualify for the rebate. The estimate rebate for these taxpayers will be $101,783,200 ($400 x 254,458).
20. This fiscal note assumes the full rebate amount will be paid in FY 2008 and 97% of the rebate will be claimed. Based on these assumptions, the impact of the rebate on the general fund in FY 2008 is $98,729,704 ($101,783,200 x 97%).
21. Taxpayers who claim an itemized deduction for property taxes on their 2006 state income tax returns would be required to report their rebates as income on their 2007 tax returns. It is assumed that all income taxpayers who itemize would be receiving $400 in rebate.
22. In 2005, 161,311 resident households claimed an itemized deduction for property taxes. Based on the 2003 growth rate for itemizers of 3%, this number is expected to grow 6% (3% x 2 years) to 170,990 (161,311 x 1.06) by 2007. These households will report their rebates as an additional $68,396,000 ($400 x 170,990) of income on the 2007 income tax returns they file in the spring of 2008.

23. In 2005, the average marginal tax rate of taxpayers who claimed an itemized deduction for property taxes was 5.88%. Taxpayers who receive rebates and took an itemized deduction for property taxes in 2006 will owe an additional $4,021,685 (5.88% x $68,396,000) when they file their 2007 income tax returns in the spring of 2008.
24. There will be administrative costs for the Department of Revenue for this credit and the renter's credit. Those costs are detailed below in the renter's credit section.

Renter's Credit

25. Section 12 provides a credit against income taxes of 3% of gross rent paid during 2006 with a maximum of $120 per dwelling unit. To be eligible, the taxpayer must be a resident for at least nine months of the tax year and rent for at least 7 months of the tax year. Taxpayers who share a dwelling unit must share the credit in proportion to the rent they paid. Taxpayers with adjusted gross income greater than $45,000 per year and households claiming the elderly homeowner/renter credit are not eligible.
26. There are 83,604 dwelling units in Montana that are rented for cash and occupied by households with household income less than $50,000 (U.S. Census Bureau, 2005 American Community Survey). Since household income includes tax exempt income, and is therefore more than adjusted gross income, this will be assumed to be the number of dwelling units where the renters are eligible for the credit.
27. The elderly homeowner/renter credit was claimed by 7,470 renter households in 2006. The number will be the same in 2007 and 2008.
28. There are 76,134 households eligible for this credit (83,604 – 7,470).
29. Not all taxpayers eligible for a credit claim it. Use of means tested programs and tax credits varies from close to zero up to two-thirds to three-fourths of eligible households. Usage of this credit is unknown, but this fiscal note assumes that the credit will be well publicized and that 70% of eligible households will claim the credit.
30. Renters with annual rent of $4,000 or more ($120 / 3%) will claim the maximum credit of $120.
31. Rental units with annual rent of $4,000 or more make up 86% of the total. The average rent of rental units with rent less than $4,000 is $2,385. (U.S. Census Bureau, 2005 American Community Survey)
32. The average credit claimed by occupants of a rental unit will be $113 (86% x $120 + 14% x $2,385 x 3%).
33. There will be 53,294 households who claim the credit (70% x 76,134). Total credits will be $6,022,222 (53,294 x $113). Credits will be claimed on tax returns filed in the spring of FY 2008. General fund revenue will be reduced by $6,022,222 in FY 2008.
34. The Department of Revenue will hire 76 temporary employees to administer the property tax rebate and renter's credit programs. Personal services costs for these employees would be $280,324. Associated operating costs would be $78,917 and equipment costs would be $6,050. Computer systems costs would be $300,000. The cost of developing forms, printing, and mailing forms, rebate checks, and 1099Gs would be $580,426. Total costs for the department to administer the property tax rebate and renter's credit programs would be $1,245,717 in FY 2008.

Income Tax Withholding on Mineral Royalties

35. Under current law, owners of Montana mineral interests pay the income tax they owe on mineral royalties only if they choose to file a Montana income tax return and report their royalty income. Sections 13 through 24 would require mineral producers to withhold 6% of mineral royalty payments to taxable parties who they pay $2,000 or more in royalties per year.
36. The Department of Revenue analyzed 2004 payments to taxable individuals reported by one of the larger oil and gas producers, and compared those payments to Montana income tax returns for 2004. Of these royalty payments:
    a. 25.5% of taxable royalties were paid to individuals and 74.5% were paid to corporations,
    b. 92.5% of payments to individuals went to persons who would be subject to withholding under this bill,

   c. 43.0% of payments to individuals went to persons who did not file Montana income tax returns, and
   d. 37.4% of payments to individuals went to persons who would be subject to withholding and did not file Montana income tax returns.

37. Of royalties paid to persons who filed income taxes, 6.8% were paid to persons who did not owe Montana income tax.
38. The average marginal tax rate of royalty recipients who filed Montana income tax returns was 6.11%.
39. The percentage of businesses receiving mineral royalties that pay taxes owed on them is unknown. To avoid over-estimating the impact of this bill, it is assumed to be high, at 95%. All business royalty recipients are assumed to receive at least $2,000 in royalties per year, but half of royalties paid to business are assumed to be paid by a business to itself (i.e. mineral producers who are also mineral rights owners paying royalties to themselves). The percentage of business royalty recipients who do not owe tax is assumed to be the same as for individuals, or 6.8%.
40. This bill would allow oil and gas producers who produce less than 100,000 barrels of oil and 500 million cubic feet of gas to provide an annual statement of royalties paid instead of withholding. Over the last twelve quarters, oil and gas producers who were above the production threshold paid 90.6% of taxable oil and gas royalties.
41. The percentages in assumptions 35 through 39 are assumed to hold for all mineral royalties. Thus, under this bill,
    a. income taxes would be withheld on 92.5% of the 25.5% of mineral royalties paid to individuals, and on 50% of the 74.5% of mineral royalties paid to businesses. In total, taxes would be withheld on 60.8% (92.5% x 25.5% + 50% x 74.5%) of taxable royalties, with 38.8% of withholding from individuals (92.5% x 25.5% / 60.8%) and 61.3% from businesses (50% x 74.5% / 60.8%),
    b. 18.75% (38.8% x 37.4% /92.5% + 61.3% x 5%) of taxes owed and withheld would not have been paid without this bill,
    c. 6.8% of taxes withheld would be refunded, and
    d. taxpayers who have tax withheld would owe additional taxes equal to 0.1% of taxes withheld ((6.11% - 6%) x (100% - 6.5%).
42. Taxable royalties were 11.8% of gross value reported on oil and gas tax returns for 2001 through 2005.
43. The gross value of oil and gas production will be $2,795,396,000 in FY 2008 and $2,492,155,000 each year in FY 2009 through FY 2010 (HJR 2).
44. Taxable oil and gas royalties paid by producers subject to withholding will be $298,850,196 in FY 2008 (90.6% x 11.8% x $2,795,396,000) and $266,431,307 each year in FY 2009 through FY 2010 (90.6% x 11.8% x $2,492,155,000).
45. Non-tribal coal production will be 37,567,700 tons in FY 2008 and 36,411,700 tons per year in FY 2009 through FY 2011 (HJR 2 coal severance tax estimate). The market price will be $10.021523 per ton (HJR 2 federal mineral royalties estimate), so that the gross value of production (price times production) will be $376,485,570 in FY 2008 and $364,900,689 each year in FY 2009 through FY 2011.
46. Royalty rates average 12.5%. Total coal royalties will be $47,060,696 in FY 2008 (12.5% x $376,485,570) and $45,612,586 per year in FY 2009 through FY 2011 (12.5% x $364,900,689). State and federal coal royalties will be $36,033,403 in FY 2008 and $29,610,173 per year in FY 2009 through FY 2010 (HJR 2 school trust and federal mineral royalties estimates).
47. Taxable coal royalties will be $11,027,293 in FY 2008 ($47,060,696 - $36,033,403) and $16,002,413 per year in FY 2009 through FY 2010 ($45,612,586 - $29,610,173).
48. The gross value of production from metal mines will be $1,024,764,685 in FY 2008 and $880,261,620 per year in FY 2009 through FY 2010. Total metal mine royalties will be $128,095,586 in FY 2008 (12.5% x $1,024,764,685) and $110,032,703 per year in FY 2009 through 2011 (12.5% x $880,261,620). There are no state or federal metal mine royalties (HJR 2 school trust and federal mineral royalties estimates) so that all of these royalties are private.

49. Total taxable royalties paid by producers subject to withholding will be $437,973,075 in FY 2008 ($298,850,196 + $11,027,293 + $128,095,586) and $392,466,423 per year in FY 2009 through FY 2011 ($266,431,307 + $16,002,413 + $110,032,703).
50. Withholding will begin in January 2008, half way through FY 2008. Withholding on royalty payments will be $7,988,629 in FY 2008 (1/2 x 6% x 60.8% x $437,973,075) and $14,317,175 per year in FY 2009 through FY 2011 (6% x 60.8% x $392,466,423).
51. Beginning in FY 2009, when taxpayers who had tax withheld file their returns, they will receive refunds of 6.8% of tax withheld over the previous calendar year and make additional payments of 0.1% of tax withheld. Net collections will be $7,988,629 in FY 2008, $13,302,311 in FY 2009 ($14,317,175 – 6.7% x ($7,988,629 + $14,317,175/2)), and $13,357,924 per year in FY 2010 and FY 2011 ($14,317,175 x (100% - 6.7%)).
52. The net increase in general fund revenue would be $1,497,868 in FY 2008 (18.75% x $7,988,629), $2,494,183 in FY 2009 (18.75% x $13,302,311), and $2,504,611 per year in FY 2010 and FY 2011 (18.75% x $13,357,924).
53. The Department of Revenue would need to add a new module to its data processing system at a cost of $300,000 in FY 2008 and with testing costs of $1,213 per year. Processing and auditing additional withholding and income tax returns would require one additional auditor and one additional administrative support position, with personal service costs of $103,923 in FY 2008 and FY 2009, increasing to $106,521 in FY 2010 and $109,184 in FY 2011. Equipment costs to set up these positions would be $11,800 in FY 2008. Operating costs would be $21,322 in FY 2008 and $22,218 in FY 2009, increasing by 2.5% per year in later years. Creating a new withholding form would have operating costs of $2,500 in FY 2008, and annual costs for mailing forms of $2,372, increasing by 2.5% in FY 2010 and FY 2011.

Reporting Requirements

54. Section 27 requires taxpayers who have used potentially abusive tax avoidance transactions, as defined by the IRS or the Department of Revenue, to report those transactions and provides penalties for failing to report them. Section 28 requires parties who have assisted taxpayers in using potentially abusive tax avoidance transactions to report those transactions and provides penalties for failure to report. Section 29 provides penalties for promoting tax shelters and assisting taxpayers in miss-stating income or tax liability. Section 35 requires corporations that file tax returns in Montana and other states to provide information from those returns to the Department of Revenue to allow the department to determine whether the information is consistent.
55. The reporting requirements and penalties in Sections 25 through 37 will increase voluntary compliance with the individual income tax and corporation license tax and will make it easier for the department to detect taxpayers who are not in compliance. Based on the size and number of cases identified using information shared by other states, this is expected to produce $3.2 million per year in additional revenue beginning in FY 2009.

Voluntary Compliance Initiative

56. Sections 38 through 40 would allow taxpayers who have used abusive tax avoidance transactions to file amended returns and pay tax due from previous years in September through December of 2007 with no civil or criminal penalties.
57. Several states have conducted similar voluntary compliance programs. Four states, California, New York, North Carolina, and Illinois provided information on the results of their programs that distinguished between payments from corporations and individuals.
58. For these states, increased individual income tax collections were divided by the highest individual marginal tax rate to give an estimate of the increase in reported taxable income. For each state, the increase in taxable income was multiplied by the ratio of Montana’s 2005 personal income to that state’s 2005 personal income to give a proportionate increase in taxable income for Montana. These were then

multiplied by the top marginal tax rate of 6.9% to give equivalent increases in Montana personal income tax revenue.

59. Similarly, increased corporation income tax collections in each of the four states was divided by that state's corporate tax rate, multiplied by the ratio of Montana's 2005 gross state product to the other state's gross state product, and then multiplied by the Montana corporation tax rate of 6.75% to give equivalent increases in Montana corporation tax revenue.
60. The total increases in Montana tax liability equivalent to the results from the four states ranged from $10.2 million to $22.5 million with an average of $16.53 million Montana differs in some ways from states that have already run programs. Therefore, it is conservatively estimated that a voluntary compliance program in Montana would be half as successful as the least successful program in the four states, producing $5.1 million in additional revenue in FY 2008.

Income Tax Withholding – Capital Gains on Nonresident Real Estate Sales

61. Sections 41 through 47 require income tax withholding for capital gains on real estate sales by nonresidents.

<u>Residential Property</u>

62. In 2005, records from the department's property tax database (CAMAS) combined with sales history file data reveal 989 class 4 real property sales by non-residents that have a sales amount of at least $100,000, with a sales total of $401,843,532.
63. Section 20 of the bill provides that the withholding amount required is either 2.5% of the sales price or the amount of the transferor's certified calculated gain multiplied by the highest rate of tax. It is assumed non-resident sellers will choose the lower of the two amounts.
64. To determine the amount of additional non-resident withholding revenue this bill will generate, the department did a study to determine the rate of non-compliance. Based on tax year 2003, business and income tax staff found that 70% of non-residents failed to file state tax returns on the gain of sales for class 4 property.
65. A random sample of 692 recorded sales, or 70%, of the 989 non-resident sales in 2005 were selected to provide data for this fiscal note. The total sales amount for these 692 records was $244,525,855.
66. Of the 989 total sales in calendar year 2005, 657 records had a previous sales amount. Based on a review of these 657 sales, the most frequent percentage gain was 47%.
67. Multiplying the $244,525,855 x 47% results in an estimated $114,927,152 in unreported capital gains on class 4 sales.
68. At a 4% tax rate (6% average income tax rate less the 2% capital gains credit), the resulting tax revenue from unreported capital gains on sales of real property is estimated as $4,597,086 ($114,927,152 X 4%).

<u>Agricultural Property</u>

69. For class 3 agricultural land, based on the property's class code, a per acre value was selected from the appropriate USDA 2005 average value per acre for the particular type of land (farm real estate, cropland, irrigated, non-irrigated, and pasture acreage). In 2005, there were 2,341 class 3 agricultural land sales by non-residents. Multiplying the acreage quantity by the appropriate USDA per acre rate resulted in estimated sales of $148,869,350.
70. A randomly selected sample of 1,639 observations was drawn from the 2005 agricultural land sales. Based on this sample, in 2005 agricultural land properties totaling $107,287,457 in sales were sold by non-residents for gains that were not reported.
71. From 1994-2004, the USDA average increase in the value of farmland was 4.93% per year for a 62% increase over 10 years. This rate was used to estimate unreported capital gains of $66,518,223 ($107,287,457 X 62%) on the agricultural land sales. Applying a 4% tax results in revenue of $2,660,729 ($66,518,223 X 4%).

Total Additional Withholding Revenues

72. Combining the anticipated unreported capital gains from class 3 and class 4 sales results in $7,257,815 in estimated revenue from sales in 2005. The Center for Applied Economic Research reports that between 1999 and 2003, the average home price increased at an annual rate of growth of 8.6%. Data maintained by the Federal Reserve Bank of Kansas City indicates fairly comparable land value changes for agricultural farmland since the first half of 2004. Therefore, this growth rate was used to estimate revenues which are projected to be $9,295,984 in FY 2008, $10,095,439 in FY 2009, and $10,963,646 in FY 2010, and $11,906,520 in FY 2011.

Lodging and Rental Car Taxes

73. Sections 93 and 97 expand the list of lodging facility or accommodations to include timeshares available for rental and vacation home rental. The definition of lodging facility or accommodations includes all facilities that provide overnight lodging facilities for periods of less than 30 days to the public for compensation. Therefore, these types of facilities are subject to lodging and accommodations tax currently. No data is available to determine if the revision will affect revenues.
74. Sections 93 through 108 clarify that fees charged by intermediaries, such as on-line reservation services, are part of the base for the lodging facility use tax, the accommodations sales tax, and the rental car sales tax.
75. The bill is effective July 1, 2007.
76. The Department of Revenue obtained quotes for rooms in Helena, Billings, Missoula, Kalispell, Bozeman, Great Falls, and Glendive through three on-line reservation services and directly from the lodging facilities. On average, the intermediaries' quotes were $8.07 higher. Intermediaries often obtain discounts from lodging operators when they book a room, so that the intermediaries' fees probably are higher. However, since the discounts intermediaries obtain are unknown, the average intermediary fee is estimated to be $8.07.
77. In 2003, the number of lodging rooms rented in Montana was 5,146,000. From 1999 to 2003, room rental grew at an average annual rate of 1.65% (Institute for Tourism and Recreation Research, University of Montana). Assuming that lodging rentals continue to grow at the same rate, rentals will number 5,540,472 in FY 2008, 5,632,160 in FY 2009, 5,725,365 in FY 2010, and 5,820,113 in FY 2011.
78. One-third of hotel rooms are booked on line (*Time* magazine, Vol. 164, 2004) and half of reservations made on line are made through an intermediary (PhoCusWright (research firm) 2004 research cited on Orbitz website). Thus, one-sixth of rooms are booked through intermediaries.
79. Taxable intermediary charges will be $7,451,935 in FY 2008 ($8.07 x 5,540,476 x 1/6), $7,575,255 in FY 2009 ($8.07 x 5,632,160 x 1/6), $7,700,616 in FY 2010 ($8.07 x 5,725,365 x 1/6), and $7,828,052 in FY 2011 ($8.07 x 5,820,113 x 1/6).

Accommodations Sales Tax

80. The rate for the accommodations sales tax is 3%, and vendors are allowed to retain 5% of taxes collected, up to $1,000 per quarter. Additional revenue will be $212,380 in FY 2008 (95% x 3% x $7,451,935), $215,895 in FY 2009 (95% x 3% x $7,575,255), $219,468 in FY 2010 (95% x 3% x $7,700,616), and $223,099 in FY 2011 (95% x 3% x $7,828,052).
81. All revenue from the accommodations sales tax is deposited in the general fund.

Lodging Facility Use Tax

82. The rate for the lodging facility use tax is 4%, and no vendor allowance is deducted. Additional revenue will be $298,077 in FY 2008 (4% x $7,451,935), $303,010 in FY 2009 (4% x $7,575,255), $308,025 in FY 2010 (4% x $7,700,616), and $313,122 in FY 2011 (4% x $7,828,052).
83. The lodging facility use tax is allocated first to pay the department's costs of administering the tax and to reimburse state agencies for taxes paid on employees' business travel.
84. State agencies are reimbursed 4% of their lodging costs. Thus, they are already being reimbursed for the tax on any intermediary fees they pay, and there will be no change in agency reimbursements.

85. To handle the increased volume and complexity of returns, the Department of Revenue would require an additional 1.00 FTE auditor and an additional 0.50 FTE for processing. The Department of Revenue will also need to upgrade its data processing system to accommodate electronic filing for lodging taxes. The estimated cost of the upgrade is $100,000 in FY 2008.
86. Additional personal services for the 1.5 FTE are estimated to be $71,221 in FY 2008 and FY 2009, increasing by 2.5% per year to $73,002 and $74,827 in FY 2010 and FY 2011 respectively. The additional operating expenses are estimated to be $140,903 in FY 2008, which also includes the cost of the computer upgrade and form development, $38,499 in FY 2009, $39,461 in FY 2009, and $40,448 in FY 2011. Additional equipment costs are estimated to be $5,900 in FY 2008. Total additional costs would be $218,024 in FY 2008 and $109,719 in FY 2009, increasing by 2.5% per year to $112,463 in FY 2010 and $115,275 in FY 2011.
87. Remaining revenue is allocated 67.5% to the Department of Commerce; 1% to the Montana Historical Society; 2.5% to the University System for the Montana Travel Research Program; 6.5% to the Department of Fish, Wildlife, and Parks; and 22.5% to regional and local nonprofit tourism organizations. Total additional revenue to these entities is $80,053 in FY 2008, $193,292 in FY 2009, $195,562 in FY 2010 and $197,847 in FY 2011. The following table provides a breakdown of the change in revenue to each entity receiving a percentage of lodging facility use tax revenue. These funds would be statutorily appropriated as currently provided in statute.

Estimated Change in Revenues

	FY 2008	FY 2009	FY 2010	FY 2011
Department of Commerce	$54,036	$130,472	$132,004	$133,547
Montana Historical Society	$801	$1,933	$1,956	$1,978
Montana Travel Research Program	$2,001	$4,832	$4,889	$4,946
Department of Fish, Wildlife, and Parks	$5,203	$12,564	$12,712	$12,860
Regional and Local Non-profit Tourism Organizations	$18,012	$43,491	$44,001	$44,516
Total	$80,053	$193,292	$195,562	$197,847

Rental Car Sales Tax

88. To estimate the average fee intermediaries charge to book a rental car on line, the Department of Revenue compared price quotes from eight rental car companies in seven Montana cities for four different types of vehicles with prices for the same vehicles quoted by three on-line intermediaries. The average difference was $1.41, or 2.39% of the pre-tax price. The actual fee is likely to be larger because the intermediaries negotiate discounts with the rental companies, but because the discounts are unknown, the average fee is assumed to be 2.39% of the pre-tax price.
89. About 48% of travelers who rent a car reserve it on line (*Travel Weekly*, September 2001). It is assumed that, as with lodging, half of on-line reservations are made through an intermediary. Thus, this bill will increase revenue by 0.574% each fiscal year (2.39% x 48% x 50%).
90. Under current law, rental car tax receipts will be $3.000 million in FY 2008, $3.131 million in FY 2009, $3.268 million in FY 2010 and $3.411 million in FY 2011. Additional revenue due to this bill would be $17,220 in FY 2008 (0.574% x $3.000 million), $17,972 in FY 2009 (0.574% x $3.131 million), $18,758 in FY 2010 (0.574% x $3.268 million), and $19,579 in FY 2011 (0.574% x $3.411 million). All rental car tax revenue is deposited in the general fund.

Department of Revenue Audit Revenues

91. Department of Revenue auditors generate an average of $500,000 per year in audit revenues. At a minimum, the additional accommodations tax auditor (see assumption 85) is assumed to generate additional revenue equal to the ongoing costs associated with audit FTE, including travel costs. Therefore additional revenues are estimated by the Department of Revenue to be $86,319 in FY 2008 and FY 2009,

increasing by 2.5% per year to $88,467 in FY 2010 and $90,879 in FY 2011. These audit revenues will be deposited into the general fund.

Total General Fund Revenues

92. Total additional revenue to the general fund is the sum of rental car tax revenue, accommodations sales tax revenue and audit revenue. Total additional revenue is:
    $315,919 in FY 2008 ($17,220 + $212,380 +$86,319),
    $320,186 in FY 2009 ($17,972 + $215,895 + $86,319),
    $326,693 in FY 2010 ($18,758 + $219,468 + $88,467), and
    $333,557 in FY 2011 ($19,579 + $223,099 + $90,879).

General Revisions to Tax Laws

93. Section 50 of this bill will amend 15-1-102, MCA, to add "disregarded entity as defined in 15-30-101" to the definition of a person.
94. Section 51 of this bill will amend 15-1-201, MCA, to state that the Department of Revenue *may* collect certain information from municipal corporations. The current law states that the Department of Revenue *shall* collect certain information from municipal corporations. The purpose of this change is to reduce unnecessary reporting by municipal corporations and still allow the collection of information that is necessary for the performance of the Department of Revenue's statutory duties. This section of the bill would require other Montana state agencies to provide the Department of Revenue with relevant taxpayer information upon request, unless this is otherwise prohibited by law. This section of the bill would require other Montana state agencies to provide confidential criminal justice information that may be evidence of fraud to appropriate Department of Revenue personnel, unless this is otherwise prohibited by law. This section would allow the Department of Revenue to exchange updated taxpayer name and address information with other state agencies, unless this is otherwise prohibited by law.
95. Section 52 of this bill would amend 15-1-216, MCA, (uniform penalty and interest) to reflect federal law. The late payment penalty for all taxes except trust taxes would be changed from 1.2% per month (12% maximum) to .5% per month (12% maximum). This penalty would not be imposed on an individual income taxpayer if the taxpayer pays at least 90% of the tax for the current year when due.
96. Section 52 subsection (2)(d)(i) will add a penalty for substantial understatement of individual income tax liability on the tax return. For subsection (2)(d)(i) substantial understatement of individual income tax liability is an amount higher than $2,500. New subsections (2)(d)(ii) through (2)(d)(iv) would add a penalty for substantial understatement of any tax or matter under 15-1-211(1)(a) other than individual income taxes, if the underpayment exceeds the lesser of 10% of the correct amount required on the return or $500,000. The penalty would be 20% of the underpayment, except in cases of fraud. The penalty for underpayment due to fraud, as defined in the IRS code, would be 75% of the underpayment.
97. Section 52 subsection (3) is amended to add "fraudulently" to persons who "purposely or knowingly" fail to file a return when due. The penalty for failure to file a return would be the greater of $1,000 or 15 percent a month, with a maximum of 75% of the tax liability. Under current law the penalty is not less than $1,000 and not more than $10,000.
98. Section 52 subsection (4)(a) will make it a felony for an individual to knowingly file, render, or sign a false or fraudulent return, or to supply false or fraudulent information with respect to return or report or investigation. The penalty upon conviction would be a fine of up to $20,000, imprisonment of up to 5 years, or both.
99. Section 52 subsection (4)(b) will make it a felony for a corporation, a partnership or other entity, an officer or employee of a corporation, a member or employee of a partnership or other entity to knowingly file, render, or sign a false or fraudulent return, or to supply false or fraudulent information with respect to return or report or investigation. The penalty upon conviction would be a fine of up to $50,000, imprisonment of up to 5 years, or both.

100. Section 60 of this bill would amend 15-30-112, MCA, (exemptions for the individual income tax) to make the definition of a qualifying child consistent with the IRS code.
101. Section 61 of this bill would amend 15-30-136, MCA, to limit the deduction for federal income taxes paid for estates and trusts to no more than $5,000. This is the same limit that individuals are allowed to deduct for the state individual income tax.
102. Section 62 of this bill would amend 15-30-144, MCA. Subsection (2) would be amended to allow an individual income taxpayer an automatic extension of up to six months after the filing date to file a return. The Department could allow a further extension with good cause. Under current law, a taxpayer is allowed an automatic extension of four months, and an additional automatic extension for two months.
103. Section 63 of this bill would amend 15-30-149, MCA, to clarify the treatment of credits and refunds resulting from overpayment of individual income taxes.
104. Section 73 of this bill would amend 15-30-301, MCA. New subsection (1)(d) would add “proceeds from real estate transactions that are required to be reported under rules or regulations of the United States department of the treasury” to the list of items that an information agent must report to the Department of Revenue when no withholding tax has been deducted.
105. Section 74 of this bill would amend 15-30-303, MCA. New subsections (8)(a)(ii) and (8)(a)(iii) would require the Department of Revenue to furnish to the Department of Justice “all information necessary for the investigation and prevention of Medicaid fraud” and “all information necessary for investigation and prevention of crimes and fraud”. New subsection (8)(i) would require the Department of Revenue to furnish to the Insurance Commissioner’s Office “information necessary for the administration of Title 33, (insurer investments). New subsection (8)(j) would require the Department of Revenue to furnish to the Office of Securities Commissioner “information necessary for the administration of Title 30, chapter 10” (securities regulation).
106. Section 84 of this bill would amend 15-31-511, MCA. Subsection (1) would make it unlawful to knowingly disclose or make known confidential corporation license tax information. Under current law, it is unlawful to disclose or make known confidential corporation license tax information, knowingly or unknowingly. New subsection (4)(c) would require the Department of Revenue to furnish to the Insurance Commissioner’s Office “information necessary for the administration of Title 33” (insurer investments). New subsection (4)(d) would require the Department of Revenue to furnish to the Office of Securities Commissioner “information necessary for the administration of Title 30, chapter 10” (securities regulation).
107. Section 87 of this bill would amend 15-35-104, MCA, (reporting required for the coal severance tax) to eliminate the requirement that a coal mine operator must report the tons of coal sold to each purchaser for each quarter.
108. Section 88 of this bill would amend 15-36-313, MCA, (estimation of oil and gas production tax in the absence of a report) to eliminate the phrase “immediately after the time has expired”. This is a routine cleanup of the language of the statute. The phrase has no substantive meaning.
109. Section 89 of this bill would amend 15-39-105, MCA, to make a reference to another statute consistent with changes in numbering resulting from another section of this bill.
110. Section 90 of this bill would amend 15-39-107, MCA, to make a reference to another statute consistent with changes in numbering resulting from another section of this bill.
111. Section 109 of this bill would amend 16-11-149, MCA, to move cigarette tax appeals from the State Tax Appeal Board to the Department of Revenue. A final ruling by the department may be appealed to the State Tax Appeal Board
112. Section 113 of this bill would amend 72-3-1006, MCA, to clarify the meaning of the statute.

Impact on Department of Revenue Expenditures:

113.The Department of Revenue would establish a tax fraud unit to administer the requirements of this bill. The tax fraud unit would consist of three FTE: one attorney, one paralegal, and one auditor. The unit would pursue criminal tax fraud and assist county attorneys in prosecuting the cases developed by the unit.

Impact on Revenue Collections:

114.Reducing the late payment penalty from 1.2% per month to 0.5% per month would significantly reduce penalty and interest revenues. The Department of Revenue has estimated that reducing the late payment penalty from 1.2% per month to 0.5% per month would decrease penalty and interest revenues by $4,125,000 in FY 2007. For purposes of this fiscal note this amount is assumed to increase at 3% per year.

115.Over the last five fiscal years, penalty and interest collected from both individual income tax and corporate license tax has averaged $8.4 million dollars per fiscal year. For the purposes of this fiscal note, it is assumed that 2% of the $8.4 million were the results of penalties for underreporting or $168,000 in underreporting penalties. Under proposed law, penalties for underreporting increase by 200%. By increasing the penalties for underreporting, income tax revenue will increase by $336,000 in FY 2008. This amount is assumed to increase at 3% per year.

116.Requiring information agents to report additional information is expected to help the Department of Revenue ensure that the proper amount of tax is withheld from non-resident sellers of property for the capital gains from the sale of Montana property.

117.The other provisions of this bill would also increase future tax collections through the discovery of tax underpayments, and through increased voluntary compliance. If the bill becomes law, the Department of Revenue and other state agencies can start the information sharing process immediately. This bill would affect many of the taxes administered by the Department of Revenue. For purposes of this fiscal analysis, only the effect on individual income tax and corporation license tax collections will be considered. Even for these two taxes, it is difficult to accurately predict the increase in collections. However, if we make some conservative assumptions, we can arrive at an estimate for the impact on future revenues. It is assumed that increased voluntary compliance and the discovery of tax underpayments will result in an increase of 0.1% (one tenth of a percent) increase in income tax collections. The collections will be made up of taxes from all open previous tax years, as well as the present tax year. The projected collections for the income taxes (individual and corporate) in HJR 2 are $922.597 million for FY 2006, $954.904 million for FY 2007, $958.336 million for FY 2008, and $1,018.378 million for FY 2009. Applying the three-year average increase from FY 2006 to FY 2009 increase to subsequent years results in projected collections of $1,050.305 million for FY 2010 and $1,082.232 million for FY 2011. The estimated increase in collections during FY 2008 would be $958,336 (0.001 x $958.336 million). The estimated increase in collections during FY 2009 would be $1,018,378 (0.001 x $1,018.378 million). The estimated increase in collections during FY 2010 would be $1,050,305 (0.001 x $1,050.305 million). The estimated increase in collections during FY 2011 would be $1,082,232 (0.001 x $1,082.232 million).

Revenue Impacts from General Revision of Tax Laws

	FY 2008	FY 2009	FY 2010	FY 2011
Increased Income Tax Revenue due to Discovery and Increased Compliance	$958,336	$1,018,378	$1,050,305	$1,082,232
Increased Income Tax Revenue due to Increased Underreporting Penalty	$336,000	$346,080	$356,462	$367,156
Decreased Revenues due to Reduction of Late Reporting Penalty from 1.2% to 0.5%	($4,125,000)	($4,248,750)	($4,376,213)	($4,507,499)
Net Impact to General Fund	**($2,830,664)**	**($2,884,292)**	**($2,969,446)**	**($3,058,111)**

Cellular Telephone System Property

118. Section 54 of this bill amends 15-6-135, MCA (class 5 property). Subsection (1)(g) is amended to specify that the property of small rural telecommunications providers that serve exclusively rural areas and towns of 5,000 permanent residents or less is class five property. Under current law, the population limit is 1,200 permanent residents. Section (4) of this statute specifies that fifty percent of the market value of new rural telecommunications property in subsection (1)(g) is exempt from taxation for the year placed in service and for the succeeding nine years. New rural telecommunications property is property placed in service after January 1, 2007.
119. Section 57 of this bill amends 1523-101, MCA, (centrally assessed property) to clarify that property used for "commercial mobile radio service as defined in 47 C.F.R. 20.3" is centrally assessed property.
120. There is no fiscal impact for these sections.

Increase Class 8 Exemption

<u>Reduction in the Taxable Value of Class 8 Property</u>

121. Sections 55 and 56 change the exemption amount for class 8 property. Under current law, the threshold exemption amount is $20,000 or less of class 8 property. The current law exemption amount is a statewide amount of class 8 property owned by an individual or business entity.
122. Effective for tax year 2008, this bill provides an exemption on the first $80,000 of market value of class 8 property owned by an individual or business entity even if the taxpayer has more than $80,000 of class 8 property. The bill also exempts personal property items with a market value of less than $100.
123. Under current law, 17,328 business entities or individuals were subject to class 8 property tax in tax year 2006. Under this bill, 10,795 class 8 business owners would be removed from the tax rolls. The total taxable value decrease, before adjusting for TIF districts and local abatement, will be $29,004,599.
124. The $864,192 in taxable value of property located in a tax increment financing (TIF) district must be removed for the calculation of the state general fund revenue loss since the 95 mill levy and 1.5 mill levy tax revenue from class 8 property is retained by the TIF district. Adjusting for TIF districts, the taxable value of class 8 property in tax year 2006 that would have been exempted under this bill is $28,140,407 ($29,004,599 – $864,192).
125. The 2.7%, or $783,124 ($29,004,599 x 0.027), of abated property tax value not collected at the local level must be added back in to calculate the general fund revenue loss.

<u>Increase in Taxable Value of Class 12 Property</u>

126. The total market value of class 12 property in Montana was $1,171,178,046 in calendar year 2006. Under current law, the tax rate is an annually calculated blended rate composed of all the tax rates applied to commercial property. For calendar year 2006, the class 12 tax rate was 3.55%. The total taxable value of class 12 property was $41,576,814 in calendar year 2006.
127. If it had been in effect, this bill would have caused the class 12 tax rate to increase to 3.58% in calendar year 2006. Therefore, the taxable value increase in class 12 property would have been $351,353 ($41,928,167-$41,576,814) in calendar year 2006 under SB 220. The class 12 tax rate is projected to remain the same through FY 2011. No class 12 property is located within tax increment financing districts. Therefore, the impact of the class 12 tax rate change would be limited to state and local government and education tax revenue.

<u>General Fund Revenue Reduction</u>

128. To calculate the future general fund revenue impacts, the taxable value reduction found in assumption 123 is reduced by the amount of taxable value from TIF districts, increased by the abated taxable value which is collected at the state level but not collected at the local government level, and grown at HJR 2 growth rates. ($29,004,599 – $864,192 + $783,124 = $28,923,531)
129. The statewide 95 mill levy and the 1.5 college of technology mill levy must be applied to the estimated taxable value of the exempt property to calculate the loss in state general fund revenue. The average

statewide mill applied to the taxable value is 95.54. The tax year 2006 revenue loss associated with the 95 and 1.5 mill levies would have been $2,763,354 ($28,923,531 x 0.09554).

130. The class 8 growth rate forecast by HJR 2 is 4.3% for FY 2008 and FY 2009. For the purposes of this fiscal note, the growth rate is assumed to be 4.3% for FY 2010 and FY 2011.
131. The class 8 revenue loss associated with the 95 and 1.5 mill levies is projected to be:
    - $3,006,112 ($2,882,178 x 1.043) in tax year 2008
    - $3,135,375 ($3,006,112 x 1.043) in tax year 2009
    - $3,270,196 ($3,135,375 x 1.043) in tax year 2010
    - $3,410,814 ($3,270,196 x 1.043) in tax year 2011
132. For class 8 property, fiscal year tax payments are not based on the prior calendar year taxable value as are other classes of property. Class 8 property not liened to real property (38%) is taxed in the spring of the calendar year. Class 8 property liened to real property (62%) is collected in the following fiscal year when the normal property tax payments are made in November and May. Therefore, FY 2008 taxable value is 62% of calendar year 2007 taxable value and 38% of calendar year 2008 taxable value, etc. The increase to the class 8 exemption threshold under this bill has a partial year impact on property tax revenue in FY 2007. The bill will cause a general fund revenue loss of:
    - $1,142,323 ($3,006,112 x 0.38)) in FY 2008
    - $3,055,232 (($3,006,112 x 0.62) + ($3,135,375 x 0.38)) in FY 2009
    - $3,186,607 (($3,135,375 x 0.62) + ($3,270,196 x 0.38)) in FY 2010
    - $3,323,631 (($3,270,196 x 0.62) + ($3,410,814 x 0.38)) in FY 2011
133. The class 12 revenue increase associated with the 95 and 1.5 mill levies is projected to be $33,664 ($351,353 x 0.09554) in FY 2009 through FY 2011.
134. The total fiscal year general fund revenue loss will be:
    - $1,142,323 in FY 2008
    - $3,021,568 ($3,055,232 - $33,664) in FY 2009
    - $3,152,943 ($3,186,607 - $33,664) in FY 2010
    - $3,289,967 ($3,323,631 - $33,664) in FY 2011

<u>University Revenue Reduction</u>

135. The statewide university 6 mill levy must also be applied to the estimated taxable value of exempt property to calculate the loss in state special revenue. TIF districts do not affect this mill levy. The tax year 2006 revenue loss association with the 6 mill levy would have been $178,726 (($28,923,531 + $864, 192) x 0.006).
136. The class 8 growth rate forecast by HJR 2 is 4.3% for FY 2008 and FY 2009. For the purposes of this fiscal note, the growth rate is assumed to be 4.3% for FY 2010 and FY 2011.
137. The class 8 revenue loss associated with the 6 mill levy will be:
    - $186,412 ($178,726 x 1.043) in tax year 2007 (no impact in tax year 2007)
    - $194,427 ($186,412 x 1.043) in tax year 2008
    - $202,788 ($194,427 x 1.043) in tax year 2009
    - $211,508 ($202,788 x 1.043) in tax year 2010
    - $220,602 ($211,508 x 1.043) in tax year 2011
138. The fiscal year class 8 university revenue loss will be:
    - $70,837 (($186,412 x 0.38) in FY 2008
    - $197,604 (($194,427 x 0.38) + ($202,788 x 0.62)) in FY 2009
    - $206,101 (($202,788 x 0.62) + ($211,508 x 0.38)) in FY 2010
    - $214,964 (($211,508 x 0.62) + ($220,602 x 0.38)) in FY 2011
139. The fiscal year class 12 university system revenue increase will be $2,108 ($351,353 x 0.006) for FY 2009 through FY 2011.

140.The total university system revenue loss will be:

- $70,837 in FY 2008
- $195,496 ($197,604 - $2,108) in FY 2009
- $203,993 ($206,101 - $2,108) in FY 2010
- $212,855 ($214,964 - $2,108) in FY 2011

<u>TIF District Revenue Reduction</u>

141.The taxable value of class 8 property within TIF districts is projected to grow 4.3%. The taxable value of TIF districts will be $901,352 ($864,192 x 1.043) in tax year 2007, $940,110 ($901,352 x 1.043) in tax year 2008, $980,535 ($940,110 x 1.043) in tax year 2009, $1,022,698 ($980,535 x 1.043) in tax year 2010, and $1,066,674 ($1,022,698 x 1.043) in tax year 2011.

142.It is assumed that the average statewide mill levy will grow at the calendar year 2000 through calendar year 2006 growth rate of 3.4%. The TIF districts do not receive the revenue from the 6 mill levy. In calendar year 2006 (FY 2007) the average statewide mill levy was 526.84. In calendar year 2007 (FY 2008) the average statewide mill levy, less the university 6 mill levy, will be 538.75 ((526.84 x 1.034) - 6). Property within a tax increment financing district is either in the TIF's base or in its' increment. For the purposes of this fiscal note it will be assumed the reduction in class 8 taxable value is taken from the value of the increment. This results in a property tax revenue reduction within TIF districts of:

- $192,465 (($901,352 x 0.38) x 0.53875) in FY 2008
- $532,460 (($940,110 x 0.62) + ($980,535 x 0.38) x 0.55727) in FY 2009
- $574,441 (($980,535 x 0.62) + ($1,022,698 x 0.38) x 0.57643) in FY 2010
- $619,725 (($1,022,698 x 0.62) + ($1,066,674 x 0.38) x 0.59623) in FY 2011

<u>Business Tax Revenue Increase</u>

143.With lower property taxes, businesses will have lower property tax expenses to deduct in calculating taxable net revenue. This bill would reduce property taxes businesses pay by:

- $6,571,293 ($1,142,323 + $73,882 + $192,465 + $5,162,623) in FY 2008
- $17,628,884 ($3,021,568 + $195,496 + $532,460 + $13,879,360) in FY 2009
- $19,044,564 ($3,152,943 + $203,993 + $574,441 + $15,113,187) in FY 2010
- $20,578,913 ($3,289,967 + $212,855 + $619,725 + $16,456,366) in FY 2011

144.Corporations that do business in Montana and other states are required to report their Montana property on their corporation license tax returns. Of this property, 66.65% was reported by corporations that had positive taxable income. It is assumed that the same proportion of total business property is owned by businesses with positive net income.

145.The corporation license tax rate is 6.75%. It is assumed that the average marginal tax rate on business income reported on individual income tax returns is also 6.75%.

146.The increase in corporate tax liability is estimated to be $295,634 ($6,571,293 x 0.6665 x 0.0675) in FY 2008, $793,101 ($17,628,884 x 0.6665 x 0.0675) in FY 2009, $856,791 ($19,044,564 x 0.6665 x 0.0675) in FY 2010, and $925,820 (20,578,913 x 0.6665 x 0.675) in FY 2011.

147.Businesses frequently use the option for an extended deadline for filing tax returns. Because of this, the changes in tax liability will be reported on tax returns filed over the course of the following fiscal year and are assumed to be received in that year.

<u>Office of Public Instruction Fiscal Impact on Expenditures</u>

148.The decrease in property tax values due to HB 833 will impact the state's obligation to fund the guaranteed tax base aid for school districts and counties.

149.Property tax values will decrease by $31 million in FY 2009 (calendar year 2008) or 1.4%. There will be a two-year guaranteed tax base aid (GTB) cost increase due to the Class 8 exemption. The guaranteed level is determined by the prior year taxable values applied against current year taxable values. The lower GTB level will apply to the lower taxable values in FY 2008 and cause decreased state contribution as districts levy more mills to compensate for the decrease in taxable value. The decrease will occur over two years increasing GTB expenditures in FY 2008 by $254,000 and in FY 2009 by $415,000 for district levies as calculated by the school funding model.

150.Countywide retirement GTB will increase $95,000in FY 2008 and $155,000 in FY 2009 based on a historical average of 28% of the costs paid by the state and FY 2006 county levies equal to $63.8 million (1.4% times 63.8 million local levies times 28%).

151. In FY 2010 and beyond the lower overall level of taxable values will not have a significant impact in statewide guaranteed tax base aid costs.

<u>Administrative Costs</u>

152.This bill would require the department to allocate the Class 8 exemption by owner. The distribution must be based on the ratio of the market value of class 8 property within a given levy district to the total market value of all class 8 property owned. This will require significant changes to current property tax databases (MODS and BEVS) and to the new Orion system under development. An additional 5.0 FTE will be needed to implement Section 55 of HB 833. For FY 2008, the cost for contracted services for the Orion change is $493,020.

153.The department would also need to conduct taxpayer education to inform taxpayers about the changes to taxation of personal property. The estimated costs are $1,000 for radio, $2,200 for television, $12,000 for statewide coordination for a total cost of $15,200 in FY 2008.

Real Estate Investment Trusts

154.Sections 58 and 76 through 78 will require Real Estate Investment Trusts (REITs) to pay taxes on income earned in Montana. Under current law, REITs do not pay taxes on the income they earn in Montana to the same degree as other businesses. This occurs because of the unique deduction that REITs enjoy under federal law for dividends they pay to their owners. The dividend paid deduction effectively eliminates most, if not all, their income tax in Montana, even though they operate in the same manner as other businesses in the state.

155.If the provisions of this bill were in place during tax year 2004, an additional $3,318,153 in income tax revenue would have been collected.

156.In reviewing tax returns from tax year 2002 through tax year 2004, it was determined that revenue from requiring REITs to pay income tax like other businesses would have grown at a rate of more than 21%.

157.Based on review of SEC filings of several large REITs that have Montana holdings, it is believed that this growth trend will continue through the next decade.

158.The revenue estimate is based on growing tax year 2004 estimated revenue at 21% rate per year through 2010. However, this high growth rate is likely to decline at some future date that is outside the time period covered by this fiscal note.

159.The department will not require any additional resources to administer this change in law.

Residential Property Tax Credit

160.Sections 64 through 72 amend the elderly homeowner/renter credit in 15-30-171 through 15-30-179, MCA, by allowing taxpayers younger than 62 to claim a credit of up to $400 and increasing the percentage of the credit allowed for taxpayers with household incomes between $35,000 and $45,000. These changes would be effective beginning with tax year 2007.

161.Currently, a high percentage of eligible homeowners with incomes between $15,000 and $25,000 take the credit, but much lower percentages of renters and homeowners with higher and lower incomes take the credit. In particular, no taxpayers with household income between $35,000 and $45,000 took the credit.

162.Making the credit available to households of all ages and increasing the credit for households with income between $35,000 and $45,000 will increase the percentage of eligible households claiming the credit. The following table shows actual participation rates in 2005 and assumed participation rates for 2007 and future years. For income groups with participation rates of more than 50%, this bill is assumed not to affect the participation rate. For income groups with participation rates less than 50% and more than 0%, this bill is assumed to increase the participation rate 1.5 times. For households with income between $35,000 and $39,999, the participation rate with this bill is assumed to equal the actual 2005 participation rate for households with income between $25,000 and $34,999. For households with income between $40,000 and $44,999, the participation rate with this bill is assumed to be half the actual 2005 participation rate for households with income between $25,000 and $34,999.

Homeowner/Renter Credit Participation Rates

	Homeowners		Renters	
Income Range	Actual 2005	Estimated Future	Actual 2005	Estimated Future
Less than $10,000	22.9%	34.3%	21.4%	32.0%
$10,000 to $14,999	39.4%	59.0%	34.7%	52.1%
$15,000 to $19,999	92.2%	92.2%	42.1%	63.2%
$20,000 to $24,999	73.6%	73.6%	11.7%	17.6%
$25,000 to $29,999	17.8%	35.6%	3.2%	4.7%
$30,000 to $34,999	17.8%	26.7%	3.2%	4.7%
$35,000 to $39,999	0.0%	17.8%	0.0%	3.2%
$40,000 to $44,999	0.0%	8.9%	0.0%	1.6%
Total	37.4%	38.8%	20.2%	27.7%

163. In 2005, total credits of $11,580,412 were claimed by elderly households. With the assumed participation rates, credits would be $26,850,371, an increase of $15,269,959.
164. Credits will be claimed on tax returns filed in the spring following each tax year. General fund revenue will be reduced by $15,269,959 per year, beginning in FY 2008.

Grantor Trust Clarification

165. Sections 58, 59, and 76 clarify how grantor trusts should be treated for income tax purposes including conditions when the reporting requirements should be waived. Under current law, there is no specific definition of how grantor trusts should be treated for tax purposes, so the Department of Revenue and tax practitioners are unsure of how to treat Grantor Trusts. This bill is likely to correct for underreporting of taxable income, thus creating a positive revenue impact. However, quantifying the impact to state general fund revenue is not possible because of the lack of previous reporting.

Coordination Between Department of Revenue and Secretary of State

166. Sections 75, 84, 85, 110, and 111 require businesses to provide their federal tax identification number on the Annual Report filed with the Secretary of State's Office and provide for sharing of this information with the Department of Revenue.
167. The Secretary of State's Office database will need to be enhanced to maintain the Federal Tax ID number and the Department of Revenue specific tax year data as defined by the bill. The one time cost to modify the existing database is $24,000. The estimated cost includes costs: to code and test modifications to the existing system used for the web interface process for accessing Corporation and LLC mainframe data; to test the application online modifications to add, change, inquiry, and update history screens; to test batch reporting enhancements; to update the current SOS database to include existing Federal Tax IDs and additional data as received from DOR; and to define security for both the SOS mainframe application and the BEAR interface process.

Changes to Water's Edge Reporting

168. Montana requires corporations that have common ownership (for example, one owns another or both are owned by a common corporate parent) and that are part of a common line of business to file a combined report. The income of members of such a "unitary group" is apportioned to Montana based on the combined income and apportionment factors of the group. This makes the income apportioned to Montana independent of financial arrangements between group members, such as the pricing of inter-company sales.
169. The normal corporation license tax rate is 6.75%. This rate is applied to the share of a corporation's worldwide income apportioned to Montana and its Montana source income. A corporation can elect to pay a higher rate of 7% and have only its United States income included in the apportionment process. This is called a "water's-edge election." When a corporation that is part of a unitary group makes a water's-edge election, some of its foreign affiliates may be excluded from the apportionment process.
170. Sections 79 through 82 make several changes to the tests for whether a foreign affiliate is included in the apportionment process of a member of a unitary group that has made a water's-edge election. It allows a corporation to rescind an existing water's-edge election beginning with the first tax period that would be affected by this bill.
    a. Under current law, domestically-incorporated affiliates are excluded from the combined reporting requirement if less than 20% of their payroll and property is in the United States. This bill eliminates this exclusion.
    b. Under current law, a subsidiary incorporated in another country must be included if more than 20% of its property and payroll is in the United States. For a foreign-owned corporation, this bill includes subsidiaries of the foreign parent corporation that meet the 20% property and payroll test.
    c. If a member of a water's edge affiliated group earns more than 20% of its income from selling services or intangibles to other members of the group, this bill would include the income and apportionment factors from those sales of services and intangibles.
    d. Under current law, any member of an affiliated group that is incorporated in a tax haven must be included in the combined report. This bill adds five countries to the list of tax havens.
    e. This bill would require that the United States income and apportionment factors of a member of a unitary group be included in the combined report if the tests for including its total income and apportionment factors are not met.
171. The Department of Revenue recalculated taxes for the largest companies with water's-edge elections for the last three tax years as if this bill had been in effect for those years. Tax liability with the provisions of this bill averaged $2.6 million per year higher than with current law.
172. The returns from the last three years did not provide information on the income and apportionment factors of some affiliates that would be included under this bill. Assuming that these corporations continued their water's-edge elections, the actual increase in revenue would be more than $2.6 million per year.
173. Corporations make the water's-edge election because it reduces their tax liability. Some corporations might find that their water's-edge tax liability under this bill is more than their regular tax liability, which is more than their water's-edge tax liability under current law. A corporation in this situation might rescind its water's-edge election. The increase in tax liability for such a corporation would be less than the amount found from recalculating its last three year's returns.
174. The impact on revenue from affiliates that were not included in recalculating returns is expected to be larger than the impact from some corporations possibly rescinding their water's-edge elections. The increase in revenue is therefore expected to be at least $2.6 million per year.
175. This bill applies to tax years beginning after December 31, 2006. The increase in revenue will first be seen in FY 2009 when corporations file their tax year 2007 returns.
176. These sections would not affect the Department of Revenue's costs of administering the corporation license tax.

Corporate License Tax Statute of Limitations

177. The statute of limitations determines the time period that the Department of Revenue may go back in auditing a taxpayer. Under current law, the statute of limitations is five years for the individual income tax and three years for the corporation license tax. This bill would make the statute of limitations five years for the corporation license tax.
178. Under current law, when the Department of Revenue audits a corporate taxpayer, it can audit the last three years' returns and any other years' returns that are being audited by the IRS. Section 83 amends Section 15-31-509, MCA so that the department would be able to audit five years' returns plus any other years' returns that are being audited by the IRS.
179. In FY 2002 through FY 2006, the department collected additional revenue or reduced refunds from an average of 23 field audits per year. On average, these audits covered returns from 3.6 years, and audit revenue averaged $83,900 for each year's return being audited.
180. Adding an additional two years of returns to 23 field audits per year would, on average, result in $3,859,400 in additional revenue (23 audits x 2 years x $83,900). With more years being open for audit, the department's audit selection tests are more likely to identify returns that should be audited in detail before those returns are past the statute of limitations. This would increase the average revenue per return. However, there would be less or no additional revenue from audits where more than three years of returns are being audited by the IRS. Also, with individual audits covering more years and no increase in audit staff, the department might average fewer field audits each year, and corporations would have an additional two years to file amended returns and ask for a refund. Thus, the additional revenue is estimated to be half this amount, or $1,929,700.
181. This bill would be effective on passage and approval, which would affect audits being conducted from the spring of 2007 forward. Because of the time between the beginning of an audit and when a taxpayer pays any resulting assessment, revenue in FY 2008 is estimated to be half the projected annual amount, or $964,850.
182. The Department of Revenue would not incur any significant additional costs because of this change.

Energy Conservation Credit

Section 86 amends 15-32-109, MCA, which provides a credit for energy conservation investments in a building. Beginning with tax year 2007, this bill

- increases the limit on the credit from $500 to $800,
- includes lighting in the investments that are eligible for the credit,
- makes the credit refundable for single taxpayers with adjusted gross income of $11,280 or less and married taxpayers with adjusted gross income of $14,590 or less, adjusted annually for inflation, and allows pass-through entities to claim the credit for investments in a residential rental building.

183. Under current law, taxpayers are allowed a credit of 25% of eligible expenditures, with the credit limited to $500. (A married couple counts as two taxpayers whether they file separate returns or a joint return.) Thus, taxpayers with eligible expenditures of $2,000 or less are unaffected by the current cap, while taxpayers with eligible expenditures of more than $2,000 are limited to a credit of $500.
184. On 2005 returns, 4,692 taxpayers claimed $500 credits. Total credits claimed by capped taxpayers were $2,346,000.
185. Based on the distribution of credits less than $500, it is assumed that each $50 increase in the cap would reduce the number of capped taxpayers 10%. It is also assumed that the average credit claimed by taxpayers who would be removed from the cap by increasing it by $50 is $25 more than the original cap. For example, increasing the cap from $500 to $550 would reduce the number of capped taxpayers from 4,692 to 4,223, and the average credit claimed by the 469 taxpayers who are capped at $500 but not at $550 would be $525.

186. With a cap of $800, 1,607 taxpayers would claim credits equal to the cap. They would claim a total of $1,285,662 in credits. There would be 3,085 taxpayers who would be capped at $500 but not at $800. They would claim a total of $2,104,615 in credits (an average of $682). Total credits claimed by taxpayers who are capped under current law would be $3,390,277, an increase of $1,044,277.
187. On 2005 returns, taxpayers who met the income requirements to have the credit refunded under this bill claimed credits that were $226,365 more than their tax liability. Under this bill, that amount would have been refunded to taxpayers.
188. There are 113,810 rental units in Montana (American Community Survey). At least half of these units are owned by individuals, who can claim the credit for investments under current law. Even with a tax credit covering part of the costs, a landlord has an incentive to invest in energy efficiency only if the landlord can recover the costs through lower energy bills or higher rents. Landlords pay for all utilities in less than 20% of units and pay for some utilities in a higher, but unknown percent of units. For this fiscal note, it is assumed that 25% of rental units are owned by pass-through entities that pay for enough of the unit's heat and other utilities to have an incentive to invest in energy conservation.
189. In 2005, credits were claimed by 5.3% of homeowners. Assuming that pass-through entity landlords will have the same participation rate on units where the landlord pays some of the utilities, they would have claimed credits on 1,508 units in 2005 (113,810 x 25% x 5.3%). Assuming that the maximum credit would be claimed for each, credits would have been $1,206,400 (1,508 x $800).
190. If this bill had been in effect in 2005, credits would have been $2,477,042 higher ($1,044,277 + $226,365 + $1,206,400).
191. Use of the energy conservation credit has grown rapidly in recent years and is expected to continue to grow. This credit is not forecast separately in HJR 2, but it accounts for a large part of a group of credits that are forecast to grow by 15.49% from 2005 to 2007, 11.23% in 2008, and 10.10% in 2009 and 2010. Assuming that the increases due to this bill will grow at the same rates, this bill would increase credits by $2,860,736 in 2007 ($2,477,042 x 115.49%), by $3,181,996 in 2008 ($2,860,736 x 111.23%), by $3,503,378 in 2009 ($3,181,996 x 110.10%), and by $3,857,219 in 2010 ($3,503,378 x 110.10%).
192. Credits will be claimed on income tax returns filed in the spring following each tax year. The increases in credits for 2007 through 2010 will result in the same reductions in revenue for FY 2008 through FY 2011.
193. Department of Revenue auditors adjust approximately 25% of the claims for this credit that they examine. With the growth in the use of this credit since it was last amended and the growth expected because of this bill, the department is not able to audit enough of the returns to ensure high taxpayer compliance with the law. To ensure adequate auditing with the increased credits, the department would need an additional half-time tax examiner with annual salary of $18,086 and annual benefits of $9,578. Total personal services costs would be $27,664 per year in FY 2008 and FY 2009, increasing by 2.5% each year in FY 2010 and FY 2011. Equipment costs to set up a new employee would be $5,900 in FY 2008. Operating costs would be $5,498 in FY 2008 and $5,946 in FY 2009, increasing by 2.5% each year in FY 2010 and FY 2011. Total additional costs would be $39,062 in FY 2008 and $33,610 in FY 2009, then increasing by 2.5% in FY 2010 and FY 2011.

Reduced License Fees for Efficient Vehicles

194. Section 112 amends 61-3-321, MCA, to exempt new light vehicles with an EPA highway fuel economy rating of at least 35 miles per gallon from the first two years' registration fees.
195. In calendar year 2006, there were 1,542 vehicles sold meeting the make and model criteria as published in the Fuel Economy Guide published by the US Department of Energy that would have qualified for the motor vehicle registration exemption provided by this bill.
196. For the purposes of this fiscal note, the number of vehicles meeting the criteria of this bill will increase 10% in FY 2008 and FY 2009 and 10% in subsequent years. The effective date of the bill, January 1, 2008, limits the FY 2008 fiscal impact to one-half year.

197. In FY 2008, 848 (1,542 x 1.10 x 0.5) vehicles will have registration fees exempted under the bill. In FY 2009, those vehicles exempted in FY 2008 will be exempted again and an additional 1,866 (1,696 x 1.1) vehicles will be exempted, totaling 2,714 vehicles. In FY 2010, 3,919 (1,866 + (1,866 x 1.1)) vehicles will be exempted. In FY 2011, 4,310 (2,052 + (2,052 x 1.1)) vehicles will be exempted.
198. The registration fee for new vehicles is $217.
199. It is estimated that general fund revenues will decrease $184,016 in FY 2008 (848 x $217), $588,938 (2,714 x $217) in FY 2009, $850,423 in FY 2010, and $935,270 in FY 2011.
200. To configure the MERLIN (Montana Enhanced Registration and Licensing Information Network) system to be in compliance with the requirements of this bill, the Department of Justice will facilitate a change order with Bearing Point/3M.
201. It is estimated that Bearing Point/3M will need approximately 228 hours to: identify the system requirements to bring the MERLIN system into compliance with this bill; develop the MERLIN system to adhere to the identified requirements; and test the system to ensure it is configured to be compliant with the requirements of this bill.
202. The estimated cost of the change order for this work to be completed by Bearing Point/3M is $34,252 to do the following:
    a. add another registration exemption reason for the mpg rating;
    b. add vehicle attributes for the mpg rating;
    c. add business rules regarding the use of the new exemption; and
    d. a user interface change for the mpg rating to be entered by the user and stored with the vehicle data in the database.
203. To program the database interface with the MERLIN system to populate the miles per gallon rating field in the vehicle maintenance module it is estimated that one database programmer will be required at approximately $80.00/hour for 120 hours totaling $9,600.

	FY 2008 Difference	FY 2009 Difference	FY 2010 Difference	FY 2011 Difference
Fiscal Impact:				
FTE				
Property Tax Refund/Renter's Credit	11.50	0.00	0.00	0.00
Mineral Royalty Withholding	2.00	2.00	2.00	2.00
Accommodations Tax	1.50	1.50	1.50	1.50
Energy Conservation Credit	0.50	0.50	0.50	0.50
General Revisions	1.50	1.50	1.50	1.50
Class 8 Exemption/Real Estate Withholding	5.00	5.00	5.00	5.00
Total FTE	22.00	10.50	10.50	10.50
Expenditures:				
Personal Services				
Property Tax Refund/Renter's Credit	$280,324	$0	$0	$0
Mineral Royalty Withholding	$103,923	$103,923	$106,521	$109,184
Accommodations Tax	$71,221	$71,221	$73,002	$74,827
Energy Conservation Credit	$27,644	$27,644	$28,335	$29,043
General Revisions	$196,718	$196,929	$201,852	$206,899
Class 8 Exemption/Real Estate Withholding	$274,176	$274,176	$281,030	$288,056
Operating Expenses				
Early Withdrawal Withholding	$1,425	$1,425	$1,461	$1,497
Property Tax Refund/Renter's Credit	$959,343	$0	$0	$0
Mineral Royalty Withholding	$327,407	$25,803	$26,448	$27,109
Accommodations Tax (DOR)	$140,903	$38,499	$39,461	$40,448
Accommodations Tax (Statutory Approps)	$80,053	$193,290	$198,305	$203,402
Sec. of State Database Modification	$24,000	$0	$0	$0
Energy Conservation Credit	$5,498	$5,946	$6,095	$6,247
Vehicle Registration Exemption	$43,852	$0	$0	$0
General Revisions	$14,151	$14,295	$14,652	$15,019
Class 8 Exemption/Real Estate Withholding	$555,930	$47,710	$48,903	$50,125
Equipment				
Property Tax Refund/Renter's Credit	$6,050	$0	$0	$0
Mineral Royalty Withholding	$11,800	$0	$0	$0
Accommodations Tax	$5,900	$0	$0	$0
Energy Conservation Credit	$5,900	$0	$0	$0
General Revisions	$11,775	$0	$0	$0
Transfers				
Guaranteed Tax Base Aid	$254,000	$415,000	$0	$0
Property Tax Refund	$98,729,704	$0	$0	$0
TOTAL Expenditures	$102,131,697	$1,415,861	$1,026,064	$1,051,856
Funding of Expenditures:				
General Fund (01)	$101,809,620	$1,112,851	$715,296	$733,180
State Special Revenue (02)	$298,077	$303,010	$310,768	$318,677
Sec. of State Proprietary	$24,000	$0	$0	$0
TOTAL Funding of Exp.	$102,131,697	$1,415,861	$1,026,064	$1,051,856

	FY 2008 Difference	FY 2009 Difference	FY 2010 Difference	FY 2011 Difference
Fiscal Impact (continued):				
Revenues:				
General Fund (01)				
Early Withdrawal Withholding	$150,000	$150,000	$0	$0
Insurance Stuffing	$1,500,000	$3,000,000	$2,250,000	$2,250,000
Property Tax Refund	$4,021,685	$0	$0	$0
Renter's Credit	($6,022,222)	$0	$0	$0
Mineral Royalty Withholding	$1,497,868	$2,494,183	$2,504,611	$2,504,611
Reporting Requirements	$0	$3,200,000	$3,200,000	$3,200,000
Voluntary Compliance Initiative	$5,100,000	$0	$0	$0
Real Estate Withholding	$9,295,984	$10,095,439	$10,963,646	$11,906,520
Accommodations & Rental Car Taxes	$315,919	$320,186	$326,693	$333,557
Water's Edge	$0	$2,600,000	$2,600,000	$2,600,000
Statute of Limitations	$964,850	$1,929,700	$1,929,700	$1,929,700
Energy Conservation Credit	($2,860,736)	($3,181,996)	($3,503,378)	($3,857,219)
Real Estate Investment Trusts	$5,970,785	$7,262,338	$8,833,269	$10,744,011
General Revisions	($2,830,664)	($2,884,292)	($2,969,446)	($3,058,111)
Vehicle Registration Exemption	($184,016)	($588,938)	($850,423)	($935,270)
Increase Class 8 Exemption	($1,142,323)	($3,021,568)	($3,152,943)	($3,289,967)
Reduced Property Tax Deductions	$0	$295,634	$793,101	$856,791
Expand Homeowner/Renter Credit	($15,269,959)	($15,269,959)	($15,269,959)	($15,269,959)
Total General Fund	$507,171	$6,400,727	$7,654,871	$9,914,664
State Special Revenue (02)				
Accomodations & Rental Car Taxes	$298,077	$303,011	$310,768	$318,677
Increase Class 8 Exemption (U System)	($73,822)	($195,496)	($203,993)	($212,855)
Total State Special Revenue	$224,255	$107,515	$106,775	$105,822
TOTAL Revenues	$731,426	$5,287,876	$7,761,646	$10,020,486
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):				
General Fund (01)	($101,302,449)	$5,287,876	$6,939,575	$9,181,484
State Special Revenue (02)	($73,822)	($195,495)	($203,993)	($212,855)

Effect on County or Other Local Revenues or Expenditures:

1. Sections 55 and 56 will have significant impacts on local governments and school district revenues if the taxable value loss is not reimbursed by the State of Montana.
2. To calculate the local governments and schools revenue impacts, the taxable value reduction of class 8 property excluding TIF districts and abated property must be used. The estimated loss in taxable value to local jurisdictions is $29,350,445 in tax year 2007, $30,612,514 in tax year 2008, $31,928,852 in tax year 2009, $33,301,792 in tax year 2010, and $34,733,769 in tax year 2011.
3. The statewide average mill levy in calendar year 2006 is 526.84 mills. Removing the state's 101.54 (95.54 + 6) mills, local governments and school have an estimated average statewide mill levy of 425.30 (526.84 – 101.54). Local government and school mills grew 4.35% annually from calendar year 2000 to calendar year 2006. This 4.35% growth is assumed to continue through FY 2011. The class 8 tax year reduction in revenue to local governments and schools will be:
   - $12,482,744 ($29,350,445 x 0.4438) in tax year 2007 (no fiscal impact in tax year 2007)
   - $13,585,850 ($30,612,514 x 0.4631) in tax year 2008
   - $14,786,439 ($31,928,852 x 0.4832) in tax year 2009
   - $16,093,124 ($33,301,792 x 0.5042) in tax year 2010
   - $17,515,281 ($34,733,769 x 0.5262) in tax year 2011
4. The class 8 fiscal year local government and school revenue loss will be:
   - $5,162,623 ($13,585,850 x 0.38) in FY 2008
   - $14,042,074 (($13,585,850 x 0.62) + ($14,786,439 x 0.38)) in FY 2009
   - $15,282,979 (($14,786,439 x 0.62) + ($16,093,124 x 0.38)) in FY 2010
   - $16,633,544 (($16,093,124 x 0.62) + ($17,515,281 x 0.38)) in FY 2011
5. The class 12 fiscal year revenue increase to local governments and schools will be:
   - $162,714 ($351,353 x 0.4631) in FY 2009
   - $169,792 ($351,353 x 0.4832) in FY 2010
   - $177,178 ($351,353 x 0.5043) in FY 2010
6. The total fiscal year revenue loss to local governments and schools will be:
   - $5,162,623 in FY 2008
   - $13,879,360 ($14,042,074 - $162,714) in FY 2009
   - $15,113,187 ($15,282,979 - $169,792) in FY 2010
   - $16,456,366 ($16,633,544 - $177,178) in FY 2011
7. Regional and local non-profit tourism promotion organizations would receive additional revenue of $17,155 in FY 2008, $43,491 in FY 2009, $44,619 in FY 2010, and $45,766 in FY 2011.

Long-Range Impacts:

1. The revenue impacts of this bill will continue after FY 2011.

Technical Notes:

1. Section 122 gives sections 58 through 72 and sections 84 through 92 a retroactive applicability date of tax years beginning after December 31, 2006. However, section 123 (6) states that section 58, sections 61 through 63, and sections 87 through 89 have an applicability date of December 31, 2007.
2. Section 122 states that section 36 applies to information on returns due on or after the date two years before the effective date of section 36 (passage and approval), except for section 36 (2) (b), which applies to any tax year for which the statute of limitations on assessment has not expired. However, section 123 states that the provisions of sections 32 through 37 (including section 36) apply to tax years beginning after December 31, 2008.

3. Section 123 (3) states that the provisions of section 37 apply to tax years *beginning* after December 31, 2008. Section 123 (4) state that the penalties imposed under section 37 apply to failure to file or provide information for tax years *ending* after the effective date of section 37. Because the effective date of section 37 is the date of passage and approval, section 123 (4) would make the penalties apply to the 2007 tax year, which appears to conflict with the applicability date of section 123 (3).
4. Both section 123 (1) and section 123 (6) provide applicability dates for section 1.

Sponsor's Initials	*Date*	*Budget Director's Initials*	*Date*